

Internal Revenue Service

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Third Party Communication: None

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Person To Contact:

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Date:

September 26, 2007

Legend:

Parent =

Sub =

LLC =

State X =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

\$a =

\$b =

\$c =

z% =

:

This letter responds to your letter dated May 17, 2007, requesting rulings as to the Federal income tax consequences of a proposed transaction. Additional information was received on September 24, 2007. The material information submitted for consideration is summarized below.

SUMMARY OF FACTS

Parent, a State X corporation, is the common parent of a group of corporations that join in filing a consolidated Federal income tax return (the "Parent Group"). Sub, a State X corporation, is wholly owned (directly and indirectly) by Parent and has been a member of the Parent Group since Date 1. LLC, a State X limited liability company whose membership interests have always been owned entirely by Sub, has been disregarded as an entity separate from Sub for Federal income tax purposes since the date of its organization (Date 4).

Between Date 2 and Date 3, Sub made multiple loans to Parent (in the aggregate amount of \$a) for Parent's general corporate purposes. Following Sub's organization of LLC, Sub contributed the Sub loans to LLC, together with an interest receivable account of approximately \$b (the "Interest Receivable Account") which represented accrued but unpaid interest on the loans. This contribution occurred on Date 5. On Date 7, (i) Parent paid cash of approximately \$c (the "Cash") to LLC in full settlement of the Interest Receivable Account and (ii) the outstanding multiple loans were consolidated into a single loan from LLC to Parent with a principal amount of \$a. The consolidation was made effective as of Date 6. The consolidated indebtedness is represented by a note with a Date 8 maturity date (the "Parent Note"). The Parent Note bears interest at a rate equal to z%, which is considered by the parties to be an arm's-length rate. That rate is reset every three months, and accrued interest for each calendar quarter is due and payable within three business days following the end of the quarter.

For what have been represented to be valid business purposes, LLC intends to become a State X corporation. LLC will make an election under Treas. Reg.

§ 301.7701-3(c) to become classified as an association (and, thus, as a corporation under § 301.7701-2(b)(2)) for Federal income tax purposes.

REPRESENTATIONS

Parent has made the following representations:

- 1) LLC is an entity that is eligible to make an entity classification election under § 301.7701-3(c)
- 2) Following LLC's entity classification election, LLC will be treated as an association for Federal income tax purposes and will become a member of the Parent Group.
- 3) Under § 301.7701-3(g)(1)(iv), the election by LLC to be treated as an association will result in Sub being treated as transferring the Parent Note and Cash to LLC in constructive exchange for shares of LLC stock (this deemed exchange transaction resulting from the entity classification election is referred to herein as the "Proposed Transaction"). The Proposed Transaction is an intercompany transaction under § 1.1502-13 that is described in § 351 of the Internal Revenue Code (the "Code").
- 4) The Parent Note constitutes indebtedness of Parent to Sub under general principles of Federal income tax law and an "intercompany obligation" under § 1.1502-13(g)(2).

LAW AND ANALYSIS

Treas. Reg. § 1.1502-13(g) (the Current Regulation) provides rules for taking into account items of income, gain, deduction, and loss of members of a consolidated group from intercompany obligations. The Current Regulation provides that if a member of a consolidated group realizes an amount (other than zero) of income, gain, deduction, or loss, directly or indirectly, from the assignment or extinguishment of all or part of its remaining rights or obligations under an intercompany obligation, then the intercompany obligation is treated for all Federal income tax purposes as satisfied under paragraph § 1.1502-13(g)(3)(ii) and, if it remains outstanding, reissued under paragraph § 1.1502-13(g)(3)(iii).

On December 21, 1998, the IRS and Treasury issued a proposed regulation under § 1.1502-13(g) (the "Proposed Regulation"). See Prop. Treas. Reg. § 1.1502-13(g), 63 Fed. Reg. 70354 (Dec. 21, 1998), 1999-1 C.B. 810. The preamble to the Proposed Regulation provides in pertinent part as follows:

“The proposed regulation clarifies the form and timing of the recast applied to transactions subject to the regulation. In particular, it clarifies that the deemed satisfaction proceeds (rather than the obligation) are treated as transferred by the initial creditor in the actual transaction and then advanced by the transferee to the debtor in the deemed reissuance of the obligation. The proposed regulation includes an example to illustrate clearly the mechanics of the proposed regulation. It also includes certain conforming adjustments.

. . . .

Proposed Effective Date

The regulation is proposed to be effective on the date that the final regulation is published in the Federal Register. For purposes of determining the tax treatment of transactions undertaken prior to such effective date, taxpayers may rely on the form and timing of the recast transaction, as clarified by these proposed regulations. No inference is intended, however, as to the correct interpretation of the existing regulation.”

RULINGS

Based solely on the information submitted and the representations set forth above, we rule as follows:

- a) Sub’s deemed exchange of the Parent Note for LLC stock is a realization event described in Treas. Reg. § 1.1502-13(g)(3)(i). The taxpayer may rely on the form and timing of the recast transaction as described in the Proposed Regulation. Accordingly, the consequences of the deemed satisfaction and reissuance will be as set forth in rulings (b) through (f) below.
- b) Immediately before it’s deemed exchange by Sub, the Parent Note will be treated as satisfied by Parent.
- c) Sub will be treated as transferring the proceeds of the deemed satisfaction to LLC in exchange for stock of LLC in an intercompany transaction.
- d) Parent will be treated as issuing a new note (the “Reissued Note”) to LLC in exchange for the proceeds of the deemed satisfaction.
- e) The Reissued Note will be deemed to have a new holding period and an issue price equal to the amount of the deemed satisfaction proceeds, but otherwise will be treated as having terms identical to those of the Parent Note.

- f) LLC's initial tax basis in the Reissued Note will equal the amount of the deemed satisfaction proceeds.

CAVEATS

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

No opinion is expressed about the tax treatment of the Proposed Transaction under other provisions of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Proposed Transaction that are not specifically covered by the above rulings.

PROCEDURAL STATEMENTS

This ruling letter is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, any taxpayer filing its return electronically may satisfy this requirement by attaching a statement to the return that provides the date and control number of this letter ruling.

In accordance with the power of attorney on file in this office, a copy of this ruling letter will be sent to your authorized representative.

Sincerely,

Michael J. Wilder
Senior Technician Reviewer, Branch 1
Office of Associate Chief Counsel (Corporate)